



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

NO POSTAGE RECEIVED
DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

DATE: [REDACTED]

SURNAME [REDACTED]

Date: NOV 14 2001

Contact Person: [REDACTED]

Identification Number: [REDACTED]

Contact Number: [REDACTED]

Employer Identification Number: [REDACTED]

Dear Applicant:

We have considered your application for recognition of exemption from federal income tax under section 501(a) of the Internal Revenue Code as an organization described in section 501(c)(7). Based on the information submitted, we have concluded that you do not qualify for exemption under that section. The basis for our conclusion is set forth below.

You were formed as a nonprofit corporation under the laws of the State of [REDACTED] on [REDACTED]. Article 3 of your incorporating instrument states that you are organized for pleasure, recreation and other nonprofitable purposes, and that you initially intend to own and operate a private membership golf club.

Article 6 of the incorporating instrument states that no part of your net earnings shall inure to the benefit of or be distributable to your members, directors, officers, or any other private person. "However, the corporation may pay reasonable compensation for services rendered to officers, directors or other persons."

Your Bylaws, dated [REDACTED], provides in Article IV that you intend to establish and operate grounds and buildings for use as a golf club (the "Club") with related amenities and activities for the Members and their guests. "The Club is intended to be an independent golf club and is not intended to be operated as a full service country club." Article IV also states that membership is designed for "purely social and recreational" purposes. "Consequently, no business may, under any circumstances, be conducted or discussed on Club property."

Bylaws, Article V, Sec. 5.2 states that the Club shall have the following classes of membership: Founding Members (Trustee Members), Honorary Founding Members, Medalist Members, Legacy Members, Regular Members, Junior Members, and Special Professional Members.

[REDACTED]

Sec. 5.2.1, Founding Members, Trustee Members, provides that this Membership category shall be available to no more than thirty (30) Founding Members. They shall be entitled to full use and enjoyment of the Club and its facilities in accordance with the Club's Bylaws and Rules.

Sec. 5.2.2, Honorary Founding Members, states that this category is available to no more than 15 Members. It is limited to those persons who were initially involved in the organization and development of the Club. These Members shall have all of the rights and obligations of Founding Members.

Sec. 5.2.3., Medalist Members, states that this class is available to no more than 55 Members. They are entitled to full use and enjoyment of the Club and its facilities in accordance with the Club's Bylaws and Rules.

Sec. 5.2.4., Regular Members, provides that these Members shall be entitled to all of the rights, interests, and privileges as set forth in these Bylaws and Club Rules. "Regular Members shall be obligated to pay dues, cart fees, and other such fees as prescribed by the Board and be subject to assessments as directed by the Board, but shall not pay green fees."

Sec. 5.2.5., Honorary Regular Members, shall have all the rights of Regular Members. The Board may also elect to suspend dues and or assessments or abolish dues and assessments for any Member in this category. In the Initial Assembly of the Club, in order for this Membership to be fully vested, such Member must bring to the Club ten new Members. There will be no more than ten such Members. If there is a capital call for the completion of the Club, these Members shall be obligated to participate on an equal basis.

Sec. 5.2.6., Legacy Members, provides that these Members shall have all the rights, privileges, and obligations of Regular Members except that such Membership shall have the privilege of naming a designated player who is approved by the Membership Committee and Board. The Designated Player may be changed as many times as requested by the Member. The Designated Player shall have the same playing and clubhouse privileges as the Legacy Member.

Sec. 5.2.7., Junior Members, is a membership category for individuals who are at least 21 years of age but under 35. They shall pay one half of regular dues and one third of the amount of any assessment. Junior Members must convert to Regular Membership prior to their 35th birthday. Junior Members shall have no vote in any Club business or election of Directors. "Junior Members, during the Initial Assembly of the Club, shall be required to bring to the Club five(5) new Members before such Junior Member is fully vested."

Sec. 5.2.8., Special Professional Members, is a membership class available to no more than ten Members. These Members are entitled to all of the rights, interests, obligations, and privileges of Regular Membership. "Special Professional Members shall pay full dues unless such Member in the prior calendar year played in at least [REDACTED] tournaments on the regular or [REDACTED] or the [REDACTED] tour or its successor tour, in which case such Special Professional Member shall pay no dues for one calendar year."

"YELLOW"

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[REDACTED]

"Special Professional Members, during the Initial Assembly of the Club, shall be required to bring to the Club ten (10) new Members before such ... Membership is fully vested."

Sec. 5.3.1., Rights Upon Dissolution, states, in part, that, "In the event of dissolution of the Club, its assets remaining after payment of all debts and expenses shall be divided equally among those non honorary Members of record and in good standing, except for Junior and Special Professional Members."

Sec. 5.4 provides, in part, that, "The Initial Assembly of the Club is that period beginning from the date on which the first organizational meeting of the Corporation is held until that date when the Club attains the membership level that the Board determines will provide for the completion and payment of the Club, its land and facilities."

In a three page document entitled "Project Information Summary", additional membership information is provided. Concerning Regular Members, the Initiation Fee begins at [REDACTED]. Dues will be \$[REDACTED] per month, which includes green fees, range fees, and baggage storage.

For Legacy Members, the Initiation Fee begins at \$[REDACTED]. This is a two-player membership, because it includes a Designated Player. This membership pays two dues (\$[REDACTED] per month total), but only one assessment, if there are any. Dues include green fees, range fees, and bag storage.

For Medalist Members, the Initiation Fee begins at \$[REDACTED]. There are no dues or assessments for the term of the membership. This membership includes green fees, range fees, and bag storage.

For Founding Members, the Initiation Fee begins at \$[REDACTED]. There are no dues or assessments for the term of the membership. Founding Members pay no guest fees or cart fees for persons playing in their foursome. Founders do not pay cart fees, range fees, or bag storage fees.

For Junior Members, the Initiation Fee begins at \$[REDACTED]. Dues will be \$[REDACTED] per month, which includes green fees, range fees, and bag storage.

For Special Professional Members, the Initiation Fee begins at \$[REDACTED]. Dues will be \$[REDACTED] per month, which includes green fees, range fees, and bag storage.

In response to Part II, 1 of Form 1024, exemption application, you state that that your activities will be as follows: the acquisition of land, construction of a golf club consisting of a golf course and related appurtenances, including a driving range and club house building, and the operation of a private golf club. Construction will commence in the third quarter of [REDACTED] and will be completed in the fourth quarter of [REDACTED]. The operation of the golf club will include activities incidental to such a facility, such as a golf pro shop and food and beverage service for its members.

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[REDACTED]

In response to Part II, 11 of Form 1024, you check off "yes" as to whether you have made, or plan to make, any payments to members or shareholders for services performed or to be performed. Your Exhibit C provides the following specific information:

Ongoing Organization, Administration, Marketing and Management Fee: Golf Management Associates, an affiliate of [REDACTED], will be paid \$[REDACTED] per month from the date of organization of the Club until 60 days after the clubhouse opens or 28 months, whichever is sooner. It will provide the following services: membership screening, membership administration, legal liaison, accounting supervision, property selection and acquisition, liaison with all consultants and contractors, and processing with all government agencies, vendor selection, accounts receivable and accounts payable, employee hiring, firing, human resources, and general management of all operations through 60 days after the opening of the clubhouse.

Grassing Expenses: [REDACTED] or one of his affiliates, will receive compensation for the purchase of sod, stolons, and seed for the grassing of the golf course. Such compensation is unknown until actual specifications for the course are determined. [REDACTED] will also provide his consulting experience in the grow-in of the fairways, roughs, and greens.

Architectural Fees: [REDACTED], an affiliate of [REDACTED] and [REDACTED], will receive \$[REDACTED] as a golf course design fee pursuant to an agreement for their architectural design services relating to the golf course and the practice area, the clubhouse site plans, clubhouse landscape plans, the maintenance building site and landscaping plans, and the entry road site and landscaping plans.

Golf Course Construction Management: [REDACTED] Inc., an affiliate of [REDACTED] and [REDACTED] will receive \$[REDACTED] as construction management fee for the construction of the golf course. This includes the cost of a full-time on-site supervisor.

Golf Design Consulting Fees: [REDACTED] will be paid a fee not to exceed \$[REDACTED] to be involved as a design consultant to [REDACTED] for the design of the course. As part of his fee, he will appear on site at least four times for membership marketing purposes.

Interior Design Consulting Fees: [REDACTED], a company owned by [REDACTED], will receive compensation of \$[REDACTED] per month for twenty-four months for interior design services for the clubhouse and for three additional years after the opening of the Club.

Marketing and Membership Sales: [REDACTED] and [REDACTED], Organizers, will receive minimum consulting fees of \$[REDACTED] each per month, plus incentive bonuses, for their services in marketing and selling memberships.

Exhibit C goes on to state that several of the Organizers will receive an Honorary Founding Membership. Such Members will have the same benefits as the Founding Members except that they will not participate in the distribution of assets upon dissolution. "The Corporation will receive no consideration for the Honorary Founding Memberships."

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[REDACTED]

In a small booklet entitled Information & Disclosure Statement, you state on Page 2 that, "Honorary Founding Members established to date are [REDACTED], [REDACTED], [REDACTED], and [REDACTED]."

The above booklet, beginning on Page 16, has a section entitled Conflicts of Interest. The opening paragraph states:

The Corporation is subject to various conflicts of interest arising out of its relationship with the Organizers and their affiliates. None of the agreements and arrangements between the Corporation and the Organizers and their affiliates, including those relating to compensation, is the result of an arm's length negotiation. These conflicts include, but are not necessarily limited to, the following:

The specific conflicts of interest described include four of the arrangements outlined under Exhibit C, to wit, the payment of \$[REDACTED] per month to [REDACTED] the \$[REDACTED] architectural fees to [REDACTED], the \$[REDACTED] contract to [REDACTED], and the \$[REDACTED] per year contract for interior design services with [REDACTED], the company owned by [REDACTED].

Paragraph No. 4 of the above section provides, in part, that, [REDACTED] and [REDACTED] will also receive compensation in the amount of 15% of the total Project Cost not to exceed \$[REDACTED], as the Developer of the Project and for its efforts in the creation of the Project concept and financial structure, assembling the Real Property, organizing the Project and the initial implementation of the Project, funding the organizing and beginning costs of the Project, marketing the memberships, and supervising the overall construction of the Project. ...No payments will be made to [REDACTED] and [REDACTED] unless the Corporation has enough money, combined with memberships subscribed, to pay all remaining budgeted Project costs as described in this paragraph."

Paragraph No. 9 states, in part, that, "The Corporation and the Organizers and their affiliates are not represented by separate counsel and it is not anticipated that they will be so represented. Therefore, there has been no separate representation concerning the compensation of the Organizers. ...Should a dispute arise, however, between the Corporation and an Organizer or any of their affiliates, or should it be necessary to negotiate and prepare contracts and agreements between the Corporation and any of the Organizers, ...the Organizers will cause the Corporation to retain counsel for such matters who has never represented the Organizer in question."

Paragraph No. 10 provides, in part, that, "Honorary Founding Members will pay no monetary consideration to the Corporation for said memberships. These have not been determined by arm's length negotiations and, therefore, result in conflicts of interest."

Section 501(c)(7) of the Internal Revenue Code provides for the exemption from federal income tax of clubs organized and operated exclusively for pleasure, recreation, and other non-profitable purposes, substantially all the activities of which are for such purposes and no part of the net earnings of which inure to the benefit of any private shareholder.

Section 1.501(a)-1(c) of the Income Tax Regulations provides that the term "private shareholders or individuals" refers to persons having a personal and private interest in the activities of the organization.

Section 1.501(c)(7)-1(a) of the regulations essentially repeats the language of Code section 501(c)(7) but also states that, in general, this exemption extends to social and recreation clubs which are supported solely by membership fees, dues, and assessments. However, a club otherwise entitled to exemption will not be disqualified because it raises revenue from members through the use of club facilities or in connection with club activities.

Rev. Rul. 70-48, 1970-1 C.B. 133, describes a nonprofit social club which has two classes of members, active and associate. Only members of a particular profession are eligible for active membership. Associate membership is open to persons whose profession, business, or activity brings them into close relationship with active members. Each associate member must be sponsored by an active member and subsequently approved by the board of governors. Associate members outnumber active members approximately four to one. Only active members have voting rights in the control of the club. Active members pay substantially lower dues and initiation fees than associate members although both classes of members enjoy the same rights and privileges in the club facilities.

Rev. Rul. 70-48 cites Code section 501(c)(7) and Rev. Rul. 58-589, 1958-2 C.B. 266, to the effect that net earnings of a club may inure to members in such forms as an increase in services offered by the club without a corresponding increase in dues or other fees paid for club support. Under the facts above, the active members receive the same club benefits as associate members, although they pay a lesser share of operating expenses. In effect, the active members are being subsidized at the expense of the associate members, which constitutes inurement of income. Held, the club is not tax exempt under section 501(c)(7) of the Code.

Concerning your own application, the evidence in the administrative file points to a discriminatory dues structure. Arguably, the differences in monthly dues, with some classes of membership altogether exempt, is set off by the fact that such classes - Founding and Medalist Members - pay higher Initiation Fees, \$[REDACTED] and \$[REDACTED] respectively, than other classes of Members. However, Honorary Founding Members have all the rights and privileges of other Founding Members, but are exempt from the payment of Initiation Fees as well as other fees, based on the representations made in your booklet entitled Information & Disclosure Statement. The seven Honorary Founding Members identified in this booklet include the initial three members of your Board of Directors - [REDACTED], [REDACTED], and [REDACTED]. Accordingly, we conclude that the holding in Rev. Rul. 70-48, cited above, is fully applicable to the facts presented in your exemption application.

"YELLOW"

[REDACTED]

Aside from the inurement which arises from the discriminatory dues structure, discussed above, the contracts and arrangements which various Organizers and their relatives or business associates have with your club also results in the inurement of your net earnings to the benefit of "private shareholders". All the Organizers (five out of seven of whom are also Honorary Founding Members) stand in the position of "private shareholders" with respect to you. See the definition in section 1.501(a)-1(c) of the regulations. The contracts and arrangements in question are for very substantial amounts, as we have detailed above. You have been forthright in stating (in the small booklet noted above) that, "None of the agreements and arrangements between the Corporation and the Organizers and their affiliates, including those relating to compensation, is the result of an arm's length negotiation." You have further stated, in this booklet, that your club and the Organizers and their affiliates are not represented by separate counsel.

While your organizing document states that you are formed for pleasure, recreation, and other nonproftable purposes, the information submitted indicates that your operations will result in the inurement of your net earnings to the benefit of "private shareholders". This is in contravention of the requirements of Code section 501(c)(7). Furthermore, the contracts and arrangements with your Organizers and Honorary Founding Members represents a substantial nonexempt purpose and conflicts with the requirement that a social club be organized and operated "exclusively" for pleasure, recreation, and other nonproftable purposes (emphasis supplied).

Accordingly, you do not qualify for exemption as an organization described in section 501(c)(7) of the Code and you must file federal income tax returns.

You have the right to protest this ruling if you believe it is incorrect. To protest, you should submit a statement of your views to this office, with a full explanation of your reasoning. This statement, signed by one of your officers, must be submitted within 30 days from the date of this letter. You also have a right to a conference in this office after your statement is submitted. You must request the conference, if you want one, when you file your protest statement. If you are to be represented by someone who is not one of your officers, that person will need to file a proper power of attorney and otherwise qualify under our Conference and Practices Requirements.

If we do not hear from you within 30 days, this ruling will become final and a copy will be forwarded to the Ohio Tax Exempt and Government Entities (TE/GE) office. Thereafter, any questions about your federal income tax status should be directed to that office, either by calling 877-829-5500 (a toll free number) or sending correspondence to: Internal Revenue Service, TE/GE Customer Service, P.O. Box 2508, Cincinnati, OH 45201.

"YELLOW"

[REDACTED]

When sending additional letters to us with respect to this case, you will expedite their receipt by using the following address:

Internal Revenue Service
[REDACTED] T:EO:RA:T:4
1111 Constitution Ave, N.W.
Washington, D.C. 20224

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

(signed) Gerald V. Sack
Gerald V. Sack
Manager, Exempt Organizations
Technical Group 4

	Initiator	Reviewer	Reviewer	Reviewer	Reviewer	Reviewer
Code	[REDACTED]	[REDACTED]				
Surname	[REDACTED]	[REDACTED]				
Date	[REDACTED]	[REDACTED]				